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NEIMAN MARCUS AND THE FIDUCIARY DUTIES OF CREDITORS' COMMITTEE MEMBERS (A/K/A "WHAT NOT TO DO")

Creditors who are members of an official committee of unsecured creditors in a bankruptcy owe fiduciary duties to other unsecured creditors and to other committee members. In this article on the Neiman Marcus bankruptcy, the authors first provide an overview of fiduciary duties in the context of committee membership. They then turn to the facts of Neiman Marcus's bankruptcy and the disastrous conduct of a committee member. They close with some lessons from the case that serve as a cautionary tale of how not to behave as a member of a committee.

By Matthew Warren, Stephen M. Blank and Jake Jumbeck *

In the chapter 11 case of Neiman Marcus, the actions taken by a member of the Official Committee of Unsecured Creditors (the "Committee") appointed in the case, Marble Ridge Capital LP, through its managing partner and principal, Daniel Kamensky, was a clear violation of the fiduciary duties that Marble Ridge voluntarily undertook, and owed, to other general unsecured creditors, as a member of the Committee. Using Marble Ridge (and Kamensky) as a cautionary tale, this article explores the intersection, and balancing, of Committee membership and fiduciary duties. Part I of this article provides an overview of fiduciary duties in the context of committee membership, Part II details the facts and circumstances of Neiman Marcus's bankruptcy cases and Marble Ridge's actions, and Part III highlights lessons and considerations.

I. FIDUCIARY DUTIES OF COMMITTEE MEMBERS

A committee of unsecured creditors is a fiduciary body appointed by the United States trustee in accordance with section 1102 of title 11 of the United States Code.[1] Such committees are designed to represent a cross-section of the applicable, unsecured creditor body and service on a committee is entirely voluntary.[2]

1 Section 1102 provides, in relevant part, that the U.S. Trustee shall appoint a committee "as soon as practicable." 11 U.S.C. § 1102(a)(1).

2 3 THE UNITED STATES TRUSTEE PROGRAM POLICY AND PRACTICES MANUAL, ¶ 3-4.2.1, at 38.

* *MATTHEW WARREN is a partner in King & Spalding LLP's Chicago office. STEPHEN BLANK is a senior associate in the firm's New York Office. JAKE JUMBECK is an associate in the firm's Chicago office. The views and opinions expressed in this article are solely those of the authors. Their e-mail addresses are mwarren@kslaw.com, sblank@kslaw.com, and jjumbeck@kslaw.com.*

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Practically, to form a committee, the U.S. Trustee first solicits the applicable debtor's largest unsecured creditors (depending on the size of a case, this initial outreach could extend to a debtor's top 20 (or more) unsecured creditors) to gauge interest in serving on the committee, although any creditor can reach out to the U.S. Trustee about serving on the committee. The U.S. Trustee, among other things, transmits a questionnaire that highlights that committee members are fiduciaries, and seeks information and representations about the creditor and its connection to the debtor.[3] Thereafter, the U.S. Trustee will either conduct phone interviews or convene a formation meeting at which it will interview those creditors who (1) attend and (2) seek to serve on the committee.[4]

Once formed and appointed, the committee owes duties, including the duties of care, loyalty, good faith, and candor, to all unsecured creditors in an applicable bankruptcy case.[5] Accordingly, each member of the committee similarly owes fiduciary duties to all unsecured creditors, as well as to the other committee members.[6]

The committee and its members do not owe fiduciary duties to the estate as a whole.[7] A committee, as a fiduciary, has a duty to maximize *unsecured* creditor recovery.[8] As such, the Committee is expected to take an adversarial approach with the debtors and/or secured creditors (as appropriate) — not to be a passive conduit for the debtor's view of the case.

However, the duty to maximize unsecured creditors' recovery, and the committee member's role as a fiduciary, must be weighed against a member's self-interest, including with respect to its own specific claims against the debtors, and ability to act in accordance with the same. Imposing fiduciary obligations is meant to "constrain what might otherwise be permissible, self-interested behavior" inherent in any committee.[9] Conceptually, each unsecured creditor (committee member or not) has an inherent conflict with one another because (absent a full recovery for all) each is competing with one another in a bankruptcy for a finite amount of assets (i.e., by eliminating a claim, a creditor directly increases the recovery to remaining creditors). Simply put, "[a]lthough Committee members owe fiduciary duties, they are hybrids who serve more than one master. Every member of the Committee is, by definition, a creditor. Thus, he is competition with every other creditor for a piece of a shrinking pie."[10]

Given that dual role, courts have recognized that each committee member has the right to look out for its own interests and may do so without violating its fiduciary duties.[11] However, members of a committee "may not

[3] The U.S. Trustee, among other things, also transmits an information sheet regarding Committee service, highlighting that "[m]embers of the Committee are fiduciaries who represent all unsecured creditors as a group without regard to the types of claims which individual unsecured creditors hold against the debtor." *Id.* Ex. D, https://www.justice.gov/sites/default/files/ust/legacy/2014/11/07/Chapter_11_Manual_Appendix_3_4_2_1.pdf.

[4] *Id.* ¶ 3-4.2.1, at 38–39.

[5] *See, e.g., Official Comm. of Equity Sec. Holders v. Official Comm. of Unsecured Creditors* (*In re Adelphia Commc'ns Corp.*), 544 F.3d 420, 424 n.l (2d Cir. 2008) (citation omitted); *Smart World Techs., LLC v. Juno Online Servs. Inc.* (*In re Smart World Techs., LLC*), 423 F.3d 166, 175 n.12 (2d Cir. 2005) (citation omitted); *Westmoreland Human Opportunities, Inc. v. Walsh*, 327 B.R. 561, 573 (W.D. Pa. 2005) (outlining the fiduciary duties owed).

[6] *Rickel & Assocs. Inc. v. Smith* (*In re* Rickel & Assocs., Inc.), 272 B.R. 74, 100 (Bankr. S.D.N.Y. 2002); *Krafsur v. UOP* (*In re* El Paso Refinery, L.P.), 196 B.R. 58, 74 (Bankr. W.D. Tex. 1996).

[7] *See, e.g., Adelphia Commc'ns*, 544 F.3d at 424 n.l (citation omitted) (noting that a committee does not owe fiduciary duties to "the debtor, other classes, or the estate").

[8] *Motorola, Inc. v. Official Comm. of Unsecured Creditors* (*In re Iridium Operating LLC*), 478 F.3d 452, 466 (2d Cir. 2007) (citations omitted).

[9] *In re ShoreBank Corp*., 467 B.R. 156, 161 (Bankr. N.D. Ill. 2012) (citing *In re Nationwide Sports Distribs*., 227 B.R. 455, 463–64 (Bankr. E.D. Pa. 1998)).

[10] *Rickel & Assocs.*, 272 B.R. at 100.

[11] *See, e.g., id.*; *Krafsur*, 196 B.R. at 74 ("[E]ach committee member also has a legitimate right to look out for its own interests, both in its capacity as a creditor with a claim against

use their positions as committee members to advance only their individual interest."[12]

II. NEIMAN MARCUS, MARBLE RIDGE, AND CROSSING THE FIDUCIARY LINE

> This conversation never happened. . . . It's too late now. They're going to report this to the U.S. Attorney's Office, okay? . . . If you're going to go to continue to tell them what you just told me, I'm going to jail, okay? *Because they're going to say that I abused my position as a fiduciary, which I probably did, right? Maybe I should go to jail.* But I'm asking you not to put me in jail.[13]

The above excerpt from a recorded telephone call between Kamensky, managing partner and principal of Marble Ridge, and the head of distressed trading ("JE1")[14] at Jefferies Financial Group, Inc. ("Jefferies"), on July 31, 2020, vividly captures the ethical dilemma, and foreshadows the ultimate conclusion of Marble Ridge's saga with, and investment in, Neiman Marcus. That investment sent Marble Ridge and Neiman Marcus on a multi-year collision course that resulted in Marble Ridge incurring over $3.5 million in legal fees,[15] the ultimate liquidation of Marble Ridge and Kamensky pleading guilty to one count of bankruptcy fraud.

A. Background

Neiman Marcus (the "Company") was a storied luxury fashion retailer founded in 1907 in Dallas, Texas. In 2013, Ares Capital and the Canadian Pension Plan Investment Board (collectively, the "Sponsors") purchased the Company for about $6.0 billion. In part, to diversify from traditional brick and mortar retail, in 2014 the Company purchased MyTheresa, a German luxury e-commerce platform.

Kamensky was a former bankruptcy lawyer at a large law firm turned hedge fund professional. He founded Marble Ridge in 2016 as a self-described "value-oriented and opportunistic distressed" hedge fund that "invest[s] across the capital structure in event- and process-driven situations."[16] In the Summer of 2018, Marble Ridge acquired certain of the Company's unsecured notes.

In September 2018, the Company disclosed that it had distributed substantially all of the equity in MyTheresa to its ultimate parent, Neiman Marcus Group Inc. — outside the reach of the Company's creditors — by utilizing a provision in its credit documents permitting dividends of unrestricted subsidiaries' equity.[17] In response, Marble Ridge began a public campaign against the transaction, alleging that the MyTheresa transaction was a fraudulent transfer and breached the applicable indenture. That public campaign was followed by, among other things, two state court actions against the Company.[18]

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footnote continued from previous page…

the estate, and in its larger role in the business community, where its primary concern and responsibility is to its own bottom line."); *see also In re Microboard Processing, Inc.*, 95 B.R. 283, 285 (Bankr. D. Conn. 1989) ("It is axiomatic that each unsecured creditor has a conflict with every other unsecured creditor in the sense that, absent a 100% distribution, the elimination or reduction of any such claim will benefit all others.").

[12] *In re ABC Auto. Prods. Corp*., 210 B.R. 437, 441 (Bankr. E.D. Pa. 1997).

[13] Statement of the Acting United States Trustee Pursuant to Court Order Regarding the Conduct of Marble Ridge Capital LP & Dan Kamensky at 22, *In re Neiman Marcus Group LTD, LLC, et al*., No. 20-32519 (DRJ) (Bankr. S.D. Tex. Aug. 19, 2020), ECF No. 1485 (emphasis added) (hereinafter, "UST Report").

[14] JE1's name has been reported in other publications. The authors decided, however, not to include JE1's name in this Article because, to their knowledge, JE1's name was not disclosed in a public filing in the bankruptcy court.

[15] *See* UST Report, *supra* note 13, at 16.

[16] MARBLE RIDGE CAPITAL LP, https://marbleridgecap.com/ (last visited Feb. 14, 2021).

[17] Additional information regarding liability management transactions generally is available on King & Spalding's Private Credit & Special Situations Investing Hub mobile app, *The Hub*, which can be downloaded from the Apple or Android app store.

[18] One action was dismissed because Marble Ridge did not have standing. Order Granting Defendants' Plea to the Jurisdiction and Alternatively, Special Exceptions, *Marble Ridge Capital LP, et al. v. Neiman Marcus Group, Inc., et al*., Cause No. DC-18-18371 (116th Judicial Dist., Dallas, Cty., Tex., Mar. 19, 2019). The other lawsuit was stayed when the Company for bankruptcy by operation of the automatic stay. 11 U.S.C. § 362(a).

B. The Company Files for Bankruptcy and Marble Ridge's Undoing

On May 7, 2020, the Company filed for bankruptcy in the Southern District of Texas in the jointly administered case captioned *In re Neiman Marcus Group LTD, LLC, et al.*, No. 20-32519 (DRJ) (Bankr. S.D. Tex.). That same day, the U.S. Trustee sent a committee solicitation package to the Company's largest creditors, which included Marble Ridge.[19] Marble Ridge completed and submitted a questionnaire expressing its desire to serve on the Committee, went through the Committee formation process detailed above, and was selected to join the Committee, which was formed on May 19, 2020.[20] Marble Ridge was subsequently chosen as one of the Committee's three co-chairs.[21]

After investigations by the Committee and the Company's disinterested directors concerning claims against the Sponsors relating to the MyTheresa transaction, the parties entered into a global settlement resolving estate claims relating to the transaction. As part of that settlement, Neiman Marcus Group Inc. would contribute 140 million shares of Series B preferred shares in MyTheresa to the Debtors' estates, which would then be contributed for ultimate distribution to non-deficiency general unsecured claim holders. In part to create liquidity for the recipients of such shares, Marble Ridge agreed to back stop the purchase of 60 million Series B shares at $0.20 per share (which effectively means Marble Ridge would purchase such shares for $0.20 from holders seeking to sell). On July 31, 2020, Jefferies contacted the Committee's financial advisor and indicated an interest in purchasing all 140 million Series B shares for a proposed purchase price in "the thirties."[22]

When the Committee informed Kamensky of the overture, that same day, July 31, 2020, Kamensky sought to leverage his business relationship with Jefferies, directing the bank, via a series of Bloomberg messages and phone calls, to "stand down," rather than make a competing offer for the Series B shares.[23] Specifically, he exchanged Bloomberg chats with JE1, including saying "DO NOT SEND IN A BID,"[24] which led to a phone call during which Kamensky threatened to pull Marble Ridge's business with Jefferies if the bank did not withdraw the MyTheresa bid.[25]

That same day, July 31, 2020, Jefferies declined to ultimately make a bid and informed the Committee that its decision not to bid was at the request of Kamensky. The Committee thereafter reached out to Marble Ridge's outside counsel, who reached out to Kamensky, regarding the allegation that Kamensky interfered with a third parties' bid for the Series B shares. Kamensky claimed that there was "a misunderstanding about his intentions," but later that day attempted "damage control," calling JE1 to plead his case. That conversation was recorded and captured the quotation that began this section.

Thereafter, the Committee disclosed Kamensky's conduct to the U.S. Trustee. On August 19, 2020, the U.S. Trustee laid out its findings in its *Statement of the Acting United States Trustee Pursuant to Court Order Regarding the Conduct of Marble Ridge Capital LP and Dan Kamensky*. The U.S. Trustee concluded that "on July 31, 2020, Marble Ridge, through Mr. Kamensky, breached its fiduciary duty of loyalty to the creditors it represented by coercing an outside investor to refrain from bidding against Marble Ridge on a key transaction that was considered integral to a successful reorganization."[26] The next day, on August 20, 2020, Marble Ridge resigned from the Committee and informed its investors that it was liquidating its funds.[27]

In the wake of the UST Report, Marble Ridge and Kamensky were the focus of various civil and criminal suits, including, (1) On August 26, 2020, the Company filed a complaint against Marble Ridge seeking, among other things: compensatory damages, subordination of Marble Ridge's claims to other general unsecured claims, and a multi-million dollar fine and (2) on September 3, 2020, Kamensky was arrested and charged by United States Attorney's Office for the Southern District of New York for fraud in the offer or sale of

[19] UST Report, *supra* note 13, at 6.

[20] *Id.* at 6–7.

[21] *Id.* at 7.

[22] *Id.* at 11.

[23] *See, e.g.*, *id.* at 13, 16, 20.

[24] *Id.* at 14.

[25] *Id.* at 16 ("Finally, Mr. Kamensky stated that he had been a good partner to JE1 and Jefferies, but if JE1 moved forward with the Series B bid, they would not be partners going forward.").

[26] *Id.* at 2.

[27] *Id.* at 25; *see* Lawrence Delevingne, *Marble Ridge to liquidate funds after Neiman Marcus scandal: letter*, REUTERS (Aug. 20, 2020, 9:58 PM), https://www.reuters.com/article/us-hedgefunds-marble-ridge-idUSKBN25H08M.

securities, extortion, bribery, and obstruction of justice, each of which carries a 5–20 year maximum sentence.

On September 25, 2020, the Company announced an agreement in principle with respect to its claims against Kamensky and Marble Ridge. The terms of the deal included Kamensky agreeing to (1) never serve on another creditors' committee; (2) reimburse $1.4 million to the debtors' estates for fees and costs incurred to date; (3) subordinate Kamensky's 2.15% interest in the Marble Ridge Master Fund to the interests of other creditors; (4) donate $100,000 to charity; and (5) perform 200 hours of community service. The settlement did not cap the amount of loss calculated in future criminal proceedings. In approving the settlement, the Bankruptcy Court commented that it was doing so "reluctantly" and described Mr. Kamensky as a "thief . . . of the lowest character." The order was entered on December 11, 2020.[28]

On February 3, 2021, Kamensky pled guilty to one count of bankruptcy fraud, which carries a maximum sentence of five years in prison.[29] On May 7, Kamensky was sentenced to six months in prison, plus six months of supervised release under home detention and a $55,000 fine.

As for the MyTheresa shares, they were ultimately distributed directly to unsecured creditors. On January 25, 2021, MyTheresa had an IPO and is currently traded under symbol MYTE. Since its IPO, MYTE has traded in excess of $29 a share as of this writing — a far cry from the $0.20 offer that Marble Ridge initially made.

III. LESSONS FROM NEIMAN MARCUS

The circumstances that led to Marble Ridge's (and Kamensky's) undoing involved a perfect storm of facts and events, and serves as a cautionary tale. It provides a striking and unequivocal example of a committee member leveraging its position on the committee, and information obtained in connection with the same, to benefit itself at the expense of the unsecured creditor body as a whole. This clear example provides valuable lessons about the line between the fiduciary duties of committee membership and self-interest. Among the valuable lessons and considerations:

- *Identify and acknowledge conflicts and recuse yourself*. Given the dual role of a committee member, conflicts may naturally arise. When they do, identify them immediately and recuse yourself from any decision-making related thereto. This applies both in deciding whether to serve on a committee and during service. For example, in *Neiman Marcus*, Kamensky was invested — having spent millions of dollars on his crusade to unwind the MyTheresa transaction. That financial and emotional investment needed to be weighed by Kamensky in evaluating whether he thought committee membership was appropriate. Moreover, during the course of the case, once Kamensky offered to backstop the MyTheresa shares, had he insisted on being recused from any matter relating to competing bids, he probably would have avoided the events and repercussions of July 31, 2020. The situation may often not be as stark as the one in *Neiman Marcus*, though. For example, a conflict can arise if a commercial debtor-tenant proposes a plan that is better for its landlords but worse for general unsecured creditors overall. A landlord serving on the committee may need to consider recusing itself from that aspect of plan negotiations, given the push-and-pull scenario in which the landlord would find itself.

- *Be cognizant of the record created*. Communication is an art. In the context of sensitive topics like business transactions and communications with business associates, communication should be focused, targeted, thoughtful, and unemotional. Marble Ridge created a real-time record of its misconduct through immediate, off-the-cuff, and emotional statements. And as seen above, those statements helped seal Marble Ridge's, and its managing partner's, fate. Parties should be cognizant of with whom they are communicating, along with the medium of those communications, and put sufficient time, thought, and preparation into their course of action.

- *The cover-up is sometimes worse than the initial act (*i.e., *when in a hole, stop digging)*. Kamensky's actions are a striking example of making a bad situation worse. While the initial actions were wrong, and a clear breach of fiduciary duties, a calm

[28] Order Granting the Joint Motion of the Reorganized Debtors, the Liquidating GUC Trust, Daniel B. Kamensky and Marble Ridge Capital LP for Entry of an Order (I) Approving a Settlement Pursuant to Federal Rule of Bankruptcy Procedure 9019 and (II) Granting Related Relief, *In re Neiman Marcus Group LTD, LLC, et al*., No. 20-32519 (DRJ) (Bankr. S.D. Tex. Dec. 11, 2020), ECF No. 2154.

[29] UNITED STATES SENTENCING COMMISSION, GUIDELINES MANUAL, § 2B1.

and coordinated response might have mitigated the fallout. Instead, Kamensky's "spin" and attempt to get Jefferies to change its story made a bad situation worse.

IV. CONCLUSION

The *Neiman Marcus* case study is an extreme example of what not to do when serving on a committee. Committee membership has its benefits (e.g., a seat at the table, influence on the direction of the case, professional fees paid by the estate, etc.), but it also comes with responsibilities to other unsecured creditors. As such, committee membership may not be for every creditor in every situation. Accordingly, a creditor serving (or thinking of serving) on a committee must carefully weigh its responsibilities as a committee member against its own self-interest, which requires a thorough and honest assessment of the facts and circumstances of a particular situation. ■